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Supreme Court of the United States

OCTOBER TERM, A. D. 1925.

No. [redacted] 117

DANIEL V. HARKIN AND UNION BANK OF CHICAGO,
RECEIVERS, ETC.,
Petitioners,

vs.

EDWARD J. BRUNDAGE, ETC., ET AL.,
Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

PETITION FOR WRIT OF CERTIORARI.

LLOYD C. WHITMAN,
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IN THE

SUPREME COURT OF THE UNITED STATES

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DANIEL V. HARKIN AND UNION BANK OF CHICAGO,
RECEIVERS, ETC.,

Petitioners,

vs.

EDWARD J. BRUNDAGE, ETC., ET AL.,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

PETITION FOR WRIT OF CERTIORARI.

To the Honorable, the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Your Petitioners, the Union Bank of Chicago, a corporation, and Daniel V. Harkin, State court receivers of the Daniel Boone Woolen Mills, Inc., an Illinois corporation, seek the review by this Honorable Court of an order of the United States Circuit Court of Appeals for the Seventh Circuit, entered April 14, 1926 (Rec. 175; rehearing denied June 4, 1926, Rec. 208), affirming an order of the United States District Court for the Northern District of Illinois, Eastern Division, entered July 9, 1925 (Rec. 47), by which latter order the District Court overruled your petitioners', the State

court receivers', motion and petition of March 13, 1925 (R
16-22), for an order on the Federal court receiver, respo
ent Edward J. Brundage, to turn over to your petitioners,
State court receivers, property of the debtor corporation
the possession of Mr. Brundage as Federal court receiver

Saturday, February 14, 1925, a minority stockholder fi
a class bill ("in his own behalf and that of all other sto
holders and other persons interested," Rec. 49) against
debtor Illinois corporation, the Daniel Boone Woolen Mi
Inc., in the Superior Court of Cook County, Illinois (R
49-55), for the appointment of a receiver (Rec. 53, 54, 54-
to collect, conserve, and marshal assets, and meanwhile c
tinue the business of the debtor corporation (Rec. 53-5
for injunction against the defendant's officers, directo
agents, and attorneys, restraining them from conveyi
pledging, or hypothecating the assets of the company, or
any manner interfering with its business and affairs;
for general relief (Rec. 55). Broadly, the bill charges
appearance of millions of dollars of assets of the corpo
tion; that the affairs of the company are at or approach
a standstill and deadlock while present and former mana
ments engage, in the public press and elsewhere, in a c
paign of mutual vituperation destructive of the good w
and seriously threatening the solvency of the corporati
and that the present officers and directors refuse to t
action against former officers and directors who have i
gally diverted assets of the debtor corporation to their
use (Rec. 49-55).

Monday, February 16, 1925, pursuant to notice, the St
court complainant presented in the State court its mot
for the appointment of a receiver of the debtor corporat
(Rec. 55), the corporation, by its attorney, entered its
pearance (formally as defendant, but in legal effect as c
plainant, the suit being a derivative proceeding) and as
for a continuance, pledging the court and opposing cou

that "the rights of the complainant under this bill will not be affected in any way at all by allowing this matter to go over for a matter of a week or ten days" (Rec. 56), and that meanwhile the *status quo* would be preserved (Rec. 56-58). Thereupon, the State court formally entered complainant's motion and continued the same to Saturday, February 21, 1925 (Rec. 55).

Immediately on leaving the court room where he had procured the continuance, as aforesaid, the debtor corporation's attorney conferred with its president (Rec. 82), and that same afternoon, Monday, February 16, 1925, the debtor corporation, through its president, vice president, a third director, and the same attorney (the first three constituting the executive committee of the board of directors, Rec. 92), decided that a receivership of the debtor corporation was necessary but determined to procure the appointment of a receiver for the corporation by a Federal court instead of the State court (Rec. 103). Accordingly, through the same attorney, the corporation solicited an out-of-town attorney for non-resident stockholders to file suit in the Federal court (Rec. 103-104), but after consulting special counsel (Rec. 104-105), decided that instead of a stockholder's bill, a creditor's bill should be filed (Rec. 105). While the creditor's bill was in preparation at the office of this special counsel "though no party plaintiff had as yet been found" (Opinion, Rec. 173), the debtor corporation, through its attorney and its vice president, solicited the United States Worsted Sales Co. to let the debtor corporation "have his claim to turn over to" special counsel "for the protection of the company and creditors and stockholders * * *; for the purpose of having a receiver appointed in the Federal court" (Rec. 105-106), with the assurance, "somewhere along the road, that there would be no expense to his company involved" (Rec. 106).

Both the Federal court plaintiff (Rec. 55) and its attorney of record herein (Affidavit of said attorney, Rec. 112)

had actual knowledge of the pendency of the State co
case and of the fact of the appearance therein of the deb
corporation and the entry and continuance of the motion
appointment of a receiver to February 21, 1925. The cour
statement (Opinion, Rec. 171) that the plaintiff did not kn
of "the proceedings that occurred in the State court" nec
sarily, and as elsewhere in the opinion (Rec. 170-171), ref
only to the special stipulation, or pledge, by the debtor c
poration in the State court.

With actual knowledge, then, as aforesaid, the United Sta
Worsted Sales Co., on Thursday, February 19, 1925, filed
bill of complaint in the instant case (Rec. 2-9), the sa
special counsel and attorney for non-resident stockhold
acting, now, as solicitors of record herein for the plain
creditor (Rec. 9). That same day, without notice to the St
court complainant, upon voluntary appearance of the deb
corporation by the same attorney who appeared for it in
State court (Rec. 11, 55), and its confession of the bill
consent to receivership (Rec. 111), the parties secured
appointment by the Federal court of respondent Edw
J. Brundage as receiver of the debtor corporation (Rec.
14). Mr. Brundage forthwith qualified as such receiver (R
15) and took possession of the assets of the defendant deb
corporation (Rec. 139).

The Federal court bill (Rec. 2-9) charges substantially
same corporate abuses and deadlock in the defendant c
poration's affairs as does the State court bill, and, like
State court bill, is a class bill in that it prays that the ass
of the defendant corporation be declared a trust fund and
ministered "for the benefit of the plaintiff and the other cr
itors and stockholders of said defendant" (Rec. 8), and tha
receiver be appointed to operate the business of the defe
ant as a going concern to prevent injury "to the plain
and to the other creditors and the stockholders of the
fendant" (Rec. 7). It shows that the total debts of the
fendant are not over twenty per cent of its assets which

ceed its liabilities "by more than '$1,500,000.00,'" and that "said corporation is solvent" (Rec. 4).

The bill alleges that plaintiff's claim is $6,176.43 (Rec. 3), and that the defendant has approximately $6,000.00 cash on hand (Rec. 6), but neither alleges demand by plaintiff upon the defendant or that the plaintiff's claim is past or presently due. And, with all deference to the Circuit Court of Appeals (Opinion, Rec. 172), there is not a scintilla of evidence in this record as to whether, in fact, plaintiff's claim was actually due. The question turns on the face of the bill itself which alleges (Rec. 3) that "the defendant is indebted to the complainant" and speaks of "the claim of the complainant." But elsewhere in the bill (Rec. 4) the terms "indebted," "debt" and "claim," are used with reference to patently non-due obligations of the debtor company, and, without exception, whenever due items are referred to (Rec. 4-5), the fact that the items are due is expressly charged.

February 28, 1925 (Rec. 69-70), on the State court complainant's motion, entered, as aforesaid, February 18, 1925, and the intervening petition of another stockholder advising the State court of the appointment of a receiver by the Federal court and the action of the debtor corporation in procuring and consenting to that appointment, the State court appointed your petitioners, the Union Bank of Chicago and Daniel V. Harkin, receivers of the debtor corporation. The State court receivers qualified March 2, 1925 (Rec. 70).

March 13, 1925 (Rec. 16), your petitioners, the State court receivers, pursuant to orders of the State court (Rec. 69-70), filed their written motion and petition in the United States District Court for an order on the Federal court receiver to turn over the property of the debtor corporation to the State court receivers.

To and including this date, namely March 13, 1925, no creditor, stockholder or other person had intervened or become party to the Federal court proceeding (Rec. 23).

The Questions Presented.

As grounds for the issuance of the writ, your petitioner respectfully present:

I.

The decision herein is in conflict with the law established by this Court in *Palmer* v. *Texas*, 212 U. S. 118. The Court of Appeals for the Seventh Circuit bases its decision upon the erroneous ruling that in a clash between a State and Federal court over possession of identical property where the other necessary elements exist, the doctrine of arrest of property (constructive possession) is not applicable if (*a*) the formal parties plaintiff in the two suits are different, or (*b*) the suits are such that neither suit could have been brought by the plaintiff in the other.

II.

The decision herein (1926) similarly conflicts with the decisions of the Circuit Court of Appeals for the Third Circuit in *Ward* v. *Foulkrod* (1920), 264 Fed. 627, and *O'Neil* v. *Welch* (1917), 245 Fed. 261, reversing *Welch* v. *Union Casualty Co.* (1917), 238 Fed. 968, and the decisions of the Circuit Court of Appeals for the Eighth Circuit in *M'Kinney* v. *Landes* (1913), 209 Fed. 300, *Harner* v. *Hegnes* (1921), 269 Fed. 53 and *Berg* v. *Fidelity Casualty Co.* (1921), 274 Fed. 311.

III.

The decision herein is in conflict with this Court's decision in *In re Metropolitan Receivership*, 208 U. S. 90, and with prior decisions of the Court of Appeals for the Third Circuit and creates a diversity of decision between the Courts of A

peal for the Third and Seventh Circuits. The Court of Appeals for the Seventh Circuit, basing its decision herein upon the erroneous conclusion that the creditors' bill is so dissimilar in nature to the stockholder's class bill that the doctrine of arrest of property is inapplicable, misapprehends the real nature of the two suits as established by the foregoing decision of this Court.

IV.

The Federal court was without jurisdiction under Section 37 of the Judicial Code. The instant case does not really and substantially involve a dispute or controversy properly within the jurisdiction of said District Court, and the parties were improperly and collusively joined for the purpose of creating a case cognizable under the Code.

V.

Such resort as in the instant case to a Federal court to evade the jurisdiction of a State court, if sustained and maintained, will result in utter disregard of necessary mutual adjustments of power between these two independent judicial systems (*Kline* v. *Burke Construction Co.*, 260 U. S. 226, 233).

Wherefore, your petitioners pray that a writ of certiorari be issued out of and under the seal of this Court, directed to the Circuit Court of Appeals for the Seventh Circuit, commanding said Court to certify and send to this Court a full and complete transcript of the record and all proceedings of said Circuit Court of Appeals in this case, which was entitled in that Court as *United States Worsted Sales Company, a corporation, plaintiff* v. *Daniel Boone Woolen Mills, Inc., a corporation, defendant*, on appeal of Daniel V. Harkin and Union Bank of Chicago, Receiver, etc., appellants *vs.*

Edward J. Brundage, Receiver, etc., et al., appellees, to the end that said cause may be reviewed and determined by this Court as provided by law, and that your petitioners may have such other and further relief or remedy in the premises as to this Court may seem appropriate and that the said judgment of the said Circuit Court of Appeals may be reversed by this Honorable Court.

Daniel V. Hoskins and
Union Bank of Chicago, Receivers, &c.,
Petitioners

By Lloyd C. Whitman
Counsel for Petitioners

Lloyd C. Whitman

Bernhardt Frank
Counsel for Petitioners.

STATE OF ILLINOIS, }
COUNTY OF COOK, } ss.

Lloyd C. Whitman, being first duly sworn deposes and says that he is one of the counsel for the petitioners herein; that he has read the foregoing petition and knows the contents thereof, and that the same is true to the best of his knowledge and belief, except as to the matters therein stated to be alleged upon information and belief and that as to those matters he believes the same to be true; and that said petition is, in his opinion, well founded in law as well as in fact.

Lloyd C. Whitman

Subscribed and sworn to before me this 30th day of August, 1926.

Notary Public

BRIEF.

I.

A.

The opinion of the Circuit Court of Appeals in the instant case holding that if the plaintiffs in the two suits are different and the subject matter of the two suits is such that neither party could have brought the same kind of suit brought by the other, the doctrine of arrest of property does not apply, is in direct conflict with the express holding of this Court in Palmer v. Texas, 212 U. S. 118.

Palmer v. *Texas*, 212 U. S. 118, is the third of a group of three cases involving the Waters-Pierce Oil Co. Case No. 1 is *Waters-Pierce Oil Co.* v. *Texas*, 212 U. S. 86, case No. 2 is *Waters-Pierce Oil Co.* v. *Texas*, 212 U. S. 112, and case No. 3 is *Palmer* v. *Texas*, 212 U. S. 118. Case No. 1 was instituted in the State court by the State of Texas to forfeit the permit of the Oil Company (a Missouri corporation) to do business in Texas, and to recover statutory penalties. The Texas State court cancelled the company's permit to do business in the state and entered judgment against it in favor of the State for $1,623,500. The same day that the State of Texas recovered this judgment in case No. 1, it instituted case No. 2 by filing its creditors' bill reciting the judgment in case No. 1 and praying for the appointment of a receiver in aid of satisfaction of that judgment. Case No. 2, in other words, was an ordinary creditors' bill by the State of Texas against the Oil Company. Thereafter, a stockholder of the Waters-Pierce Oil Co. instituted case No. 3 by filing suit in the Federal court for distribution of the assets of the de-

fendant corporation. After the State court, in case No. 2, had appointed a receiver of the Waters-Pierce Oil Co., but before the State court receiver had taken possession of the defendant company's assets, the Federal court, in case No. 3, appointed its receiver who seized the property of the defendant company in dispute. This court held in case No. 3 (*Palmer* v. *Texas*, 212 U. S. 118) that the property in dispute was in the constructive possession of the State court, and therefore sustained the right thereto of the State court receiver.

It is thus apparent that in case No. 3 (*Palmer* v. *Texas*, 212 U. S. 118), this Court applies the doctrine of arrest of property (constructive possession) as between a stockholder's bill for distribution of assets and, on the other hand, a creditors' bill not for distribution of assets but brought for the sole purpose of enforcing an obligation to the individual creditor complainant. The only identity of parties to the two involved suits was that the same corporate owner of the property was defendant in both. The only identity of subject matter of the two involved suits was that both suits sought control of the same property. Obviously, the Federal court stockholder plaintiff could not have brought suit to enforce the State court creditor complainant's credit obligation; nor, on the other hand, could the State court creditor complainant have brought the Federal court stockholder plaintiff's suit to distribute assets. *Palmer* v. *Texas*, 212 U. S. 118, therefore is conclusive that neither differences in the formal parties plaintiff, nor the fact that the one complainant could not institute or maintain the suit brought by the other complainant goes to the applicability of the doctrine of arrest (constructive possession) of property. The decision herein of the Circuit Court of Appeals for the Seventh Circuit based upon a contrary rule of law is in conflict with the law established by this Honorable Court in *Palmer* v. *Texas*.

B.

The rule in the instant case "that if the two suits were different, there was no conflict of jurisdiction, and the Court which first acquired jurisdiction over the res by actual seizure through its receiver should retain jurisdiction," is in conflict with the weight of authority, including every decision cited by the Court of Appeals for the Seventh Circuit in support of its erroneous conclusion.

By the weight of authority, the rule of the Court of Appeals for the Seventh Circuit above quoted is applicable only:

(*a*) When the court seizing the property (the second court) is exercising an exclusive jurisdiction conferred upon it by law,—as admiralty jurisdiction, or

(*b*) When the parties to the second suit are asserting a superior prior right of possession conferred upon them by the defendant owner before the first court's jurisdiction attached,—as by prior mortgage.

The affirmative principle which these cases establish is that (subject only to EXCEPTIONS (*a*) and (*b*), *supra*) in a conflict between two courts each having jurisdiction over its own subject matter and each requiring possession of the same property for the exercise of its jurisdiction, though the cases are different, the court whose potential power to arrest the property is first properly invoked, thereby acquires control of the property superior to, and to the exclusion of, subsequent actual seizure of the same property by the other court in the suit later stated.

With these principles in mind, we proceed to analyze the cases cited in the opinion herein.

(a) Empire Trust Co. v. Brooks, 232 Fed. 641.

The Federal court case was a bill to foreclose a mortgage, the State court case a bill by a stockholder, under a Texas statute, to wind up the mortgagor corporation. The decision itself, as distinguished from the court's reasoning, is an illustration of our Exception (*b*), *supra*. The appointment of the receiver in the Federal foreclosure suit was an incident of the lien created by the mortgage itself.

From the time of the execution of a mortgage there is a potential arrest of the property of the corporation in favor of the mortgagee. The stockholder whose corporation has consented to the execution of the mortgage necessarily must enforce his rights junior to those given by the mortgage. Simple contract creditors and junior lienholders of the corporation are bound by the act of the mortgagor and are likewise junior to and subject to the primary rights under the mortgage arising out of the potential arrest of property given simultaneously with the execution of the mortgage. So, when the stockholders in the *Empire Trust Co. case* filed their bill in the State court of Texas they were asserting rights junior to, and arising after the arrest of property had already been made by the execution of the mortgage (which was the subject matter of the foreclosure proceeding in the Federal court), in favor of the party in the Federal court.

The patent applicability to the instant case of this distinction of *Empire Trust Co.* v. *Brooks* is emphasized by the decision of this Court in *Pusey & Jones* v. *Hanssen*, 261 U. S. 491, as bearing upon the relative rights of the two classes of parties.—We assume the elementary proposition that "Lower federal courts are not superior to state courts" (*Leon Bonding and Surety Co.* v. *Karatz*, 262 U. S. 77, 90).

Under *Pusey & Jones Co.* v. *Hanssen*, 261 U. S. 491, a simple contract creditor, as such, has no greater right to the appointment of a receiver than has a stockholder. Nor can a

statute giving such creditor that right bind the corporation, or any other party, in any court other than those of the state of its creation (where its charter may constitute an agreement therefor by reason of special constitutional or statutory provision). The creditor only acquires the right to a receiver under a conservation bill when, as and only if, the debtor consents thereto subsequently to the creation of his debt (*In re Metropolitan Receivership*, 208 U. S. 90). Therefore if the remedy of appointment of a receiver is given to the creditor in the Federal court after the filing of the bill in the State court, and after the incidental arrest of property thereby effected by the State court, the creditor's rights must yield to the State court power.

The erroneous reasoning of the opinion in *Empire Trust Co.* v. *Brooks*, and the acceptance of that reasoning, rather than of the decision itself, by the Circuit Court of Appeals for the Seventh Circuit in the instant case, arises from the fact that in the opinion in *Empire Trust Co.* v. *Brooks* the court overlooks the fundamental characteristics of the lien asserted in the Federal bill in that case, and (pages 647-648) inadvertently misquotes the language of this Court, purposing to quote the following from *Moran* v. *Sturges*, 154 U. S. 256, 284, but omitting the matter indicated in italics:

> "As between two courts of concurrent and co-ordinate jurisdiction, having like jurisdiction over the subject-matter in controversy, the court which first obtains jurisdiction is entitled to retain it without interference, *and cannot be deprived of its right to do so because it may not have first obtained physical possession of the property in dispute.*"

(b) Palmer v. Texas, 212 U. S. 118.

We have analyzed this case above. As shown, this decision of this Court is in conflict with the decision in the case at bar, not an authority for it.

(c) Wabash Railroad Co. v. Adalbert College, 208 U. S. 3

This case, also, involved a mortgage foreclosure under ci cumstances falling within Exception (*b*), *supra*. The Cou also held that the Federal court having acquired jurisdictio by and with the consent of the parties to the State court pr ceeding retained jurisdiction of the *res* as against the Stat court by reason of the reservation in its decree, even thoug suit had first been brought in the State court.

(d) Farmers' Loan & Trust Co. v. Lake Street Elevated R Co., 177 U. S. 51.

This Court there held that the mortgagor, by the executio of the mortgage, consented to an arrest of its property i favor of the mortgagee, and, therefore, when the mortgage filed a bill in the Federal court to enforce such arrest o property, the mortgagor could not defeat the mortgagee' right to the property by filing a bill in the State court t remove the mortgagee as trustee. So in the case at bar, th owner (Daniel Boone Woolen Mills, Inc.) having consente to an arrest by the State court, can not defeat such arre by action taken later in the Federal court.

(e) Pacific Live Stock Co. v. Oregon Water Board, 241 U. S 440.

This case is not in point because there was not prese any dispute between the courts as to the control or posse sion of the same specific property; the question was sole the right of one court to enjoin proceedings pending in a other court.

(f) Moran v. Sturges, 154 U. S. 283.

Moran v. *Sturges* is an illustration of our Exception (*b supra*. The case involved the assertion of a maritime lien, an exclusively federal jurisdiction.

Applying the foregoing principles of law to the case at bar:

(*a*) Both suits involved in the instant case the taking of possession of the same property;

(*b*) Neither court had a superior right of possession by statute or prior action of the owner of the property.

(*c*) The commencement of the suit in the State court, the motion therein for the appointment of the receiver, the appearance and action of the defendant owner in placing its property under the power of the State court, preceded the filing of the bill in the Federal court and the consent therein of the corporation defendant to the appointment of a receiver.

(*d*) Therefore the Federal court, under the later bill, could not interfere with the previously attached power of the State court to take possession of the involved property.

C.

The decision herein is contrary to the holding of this Court in Farmers Loan & Trust Co. v. Lake Street Elevated Ry. Co., 171 U. S. 51. The Circuit Court of Appeals for the Seventh Circuit fails to give to the owner's pledge to the State court its legal effect as a deposit of the property with the State court and surrender by the owner to the State court of present control of the same.

"Physical possession of the property in dispute" (*Moran* v. *Sturges*, 154 U. S. 256, 284) is not an essential of priority of right of control. In *Palmer* v. *Texas*, 212 U. S. 118, this Court held that the property in dispute was in the constructive possession of the court in which suit was first brought, although the receiver therein had merely been appointed and qualified and had not reduced the property to physical possession. At what point, short of actual appointment and

qualification of the receiver, the arrest of property is effective, we believe, has never been directly and expressly settled by decision of this Honorable Court. Neither was this precise question raised or passed upon in the instant case (Opinion, Rec. 170-171). No better statement of the underlying principles can be found than the opinion of District Judge Sibley in *Patterson* v. *Veasey*, 295 Fed. 163, wherein, after an exhaustive review of authorities, including the latest expressions of this Court on the subject (*Kline* v. *Burke Construction Co.*, 260 U. S. 222, and *Lion Bonding & Surety Co.* v. *Karatz*, 262 U. S. 77), the learned Judge, at page 165, says:

> "As to criminal cases it is settled that jurisdiction for the purposes of the rule attaches not on indictment but on arrest of the person. *In re Johnson*, 167 U. S. 120, 17 Sup. Ct. 735, 42 L. Ed. 103; *Ponzi* v. *Fessenden*, 258 U. S. 254, 42 Sup. Ct. 309, 66 L. Ed. 607, 22 A. L. R. 879. *Arrest in criminal cases corresponds to service in civil cases, whether by personal notice or by seizure of some res.* Cases strictly in *rem*, in which jurisdiction arises in the court to act at all only on seizure or attachment of the *res*, may be laid to one side. So may those involving levy of general final process in the former, plainly 'jurisdiction attaches' only on seizure; in the latter, the court has no specific property to deal with until the officer selects and levies upon it. The language used in all such cases, of course, is of actual seizure as determining. In case of receivership, however, actual seizure is an impractical test, for it might easily happen that each receiver gets first actual possession of a part of the property; whereas, control of the whole is necessary for each court to exercise its jurisdiction in the premises. We find it accordingly ruled in many cases that the prior appointment of a receiver will take precedence, though there be no actual possession taken. It is enough to cite as controlling in each of the courts here involved: *Palmer* v. *Texas*, 212 U. S. 118, 29 Sup. Ct. 230, 53 L. Ed. 435; *Inter-Southern Life Ins. Co.* v. *McQuarie*, 148 Ga. 233, 96 S. E. 424. *But the cases where prior appointment concurred with prior filing and service are not authorities to the effect that 'jurisdiction at-*

taches' only by appointing a receiver. Plainly such a rule might tend to hasty and improvident action and appointments, to appointments without hearing; might also lose to diligent creditors a choice of forum important to them, as in the case of a citizen of another state in his choice of a federal forum, and would put it in the power of a defendant by resisting one application and favoring another, to determine the priority of courts. The true rule is that the filing of the bill praying for a receiver, the sanction of it by the judge, and service in accordance with his order, perfects jurisdiction—'jurisdiction attaches' over the question of the receivership. **The appointment of the receiver does not create the jurisdiction but is the result of it. The right to take possession of the property comes from the original jurisdiction to make the appointment, and not from the appointment itself. The receivership is the assertion of the jurisdiction that has already attached and a means of exercising it."**

In *Havner* v. *Hegnes*, 269 Fed. 537, the Circuit Court of Appeals for the Eighth Circuit squarely holds that the filing of the bill of complaint, service on, or appearance of the defendant and the entry of a rule upon the defendant to show cause why a receiver should not be appointed, amounted to arrest of property.

In the instant case, the suit in the State court was instituted, the defendant appeared, the complainant's motion for the appointment of a receiver was made, formally entered, and continued to a date certain. But this is not all. When, on Monday, February 16th, 1925 (three days before the Federal court bill was even filed) the State court complainant presented in the State court his motion for the appointment of a receiver (Rec. 55), the corporation entered its appearance (formally as defendant, but in legal effect as complainant, the suit being a derivative proceeding) and asked for a continuance and pledged the court and opposing counsel that "the rights of the complainant under this bill, will not be affected in any way at all, by allowing this matter to go

over for a matter of a week or ten days'' (Rec. 56), and th
meanwhile the *status quo* would be preserved (Rec. 56-58
Thereupon, the State court formally entered complainant
motion and continued the same to Saturday, February 2
1925 (Rec. 55). This pledge by the owner of the propert
accepted and acted upon by the State court, amounted, in la
to a deposit of the property by the owner with the Sta
court and a surrender, by the owner, to the court, of prese
control of the property, subject only to a condition subs
quent, namely, the possible ultimate decision of the Sta
court not to take actual possession.

Farmers Loan & Trust Co. v. *Lake Street R. Co.*, 177 U.
51, and authorities applying the rule in mortgage foreclosu
cases (Our Exception (*b*), *supra*), establish that if the own
of property has promised control of property to one pers
he can not defeat such promise by later delivering actu
control to another person. So in the case at bar, the promi
to the stockholder and to the State court to leave control wi
the State court can not be defeated by the corporation
later delivering actual control to the Federal court.

Under *Pusey & Jones Co.* v. *Hanssen*, 261 U. S. 491, a sim
ple contract creditor, as such, has no right to possession
the property of his debtor. Any right of possession subs
quently acquired from his debtor speaks, necessarily, as
such subsequent date. Neither the Federal court plaintif
nor the Federal court receiver, was a purchaser (*Harner*
Hegnes, 269 Fed. 53, 541, last 6 lines).

II.

The decision herein (1926) conflicts with the prior decisions of the Courts of Appeal for the Third and Eighth Circuits. The Court of Appeals for the Seventh Circuit bases its decision upon the ruling, contrary to the prior rulings of the Third and Eighth Circuits, that in a conflict between a State and Federal court over possession of identical property, though the other necessary elements exist, the doctrine of arrest of property (constructive possession) is not applicable if (a) the formal parties plaintiff in the two suits are different, or (b) the suits are such that neither could have been brought by the complainant in the other.

In *Ward* v. *Foulkrod* (1920), 264 Fed. 627, the Circuit Court of Appeals for the Third Circuit holds that the doctrine of arrest of property (constructive possession) is applicable, the other necessary elements existing, when the involved suits are (as in the instant case) one, a simple contract creditor's bill and, the other, a stockholder's bill, neither of which could have been brought by the complainant in the other. To like effect are the decisions of the Third Circuit Court of Appeals in *O'Neil* v. *Welch* (1917, 245 Fed. 261, and of the Circuit Court of Appeals for the 8th Circuit in *M'Kinney* v. *Landon* 1913), 209 Fed. 300, *Havner* v. *Hegnes* (1921), 269 Fed. 337, and *Berg* v. *Fidelity Casualty Co.* (1921), 274 Fed. 311.

The contrariety of decision between the Circuit Courts of Appeal for the Seventh and Third Circuits strikingly appears from an examination of the decision of the District court in *Welch* v. *Union Casualty Co.*, 238 Fed. 968, reversed by the Circuit Court of Appeals for the Third Circuit in *O'Neil* v. *Welch*, 245 Fed. 261. This District Court decision (238 Fed. 261), in premises and conclusion, is exactly in line with, and adopts and applies the identical supposed tests adopted and applied in the decision of the Circuit Court of Appeals for the Seventh Circuit in the instant case.

So, too, is the decision herein of the Circuit Court of Appeals for the Seventh Circuit in conflict with the prior decisions of that Circuit. (See, *Gaylord* v. *Fort Wayne, N. C. R. Co.* (1874), 10 Fed. Cases, Fed case No. 5284, before Circuit Judge Drummond and District Judges Hopkins and Blodgett; and *McDowell* v. *McCormick*, 121 Fed. 651, the bills in which were filed by different judgment creditors to enforce separate individual rights, neither a class bill).

III.

The error of the Court of Appeals for the Seventh Circuit in holding that the two suits were dissimilar in nature, misconceives the true nature of the two proceedings and adopts a theory thereof contrary to the decision of this Court in In Re Metropolitan Receivership, 208 U. S. 290, and contrary to prior decision of the Court of Appeals for the Third Circuit.

Assuming, for the purposes of this Point, that in law there may be differences in suits short of our Exceptions (*a*) and (*b*), discussed under our Point I, *supra*, which render the doctrine of arrest of property (constructive possession) inapplicable, no such differences exist in the nature of the two suits involved in the instant case.

The Federal court creditors' bill admitted the solvency of the debtor corporation. The substantial ground set out for relief was the inability of the debtor to pay claims then due because of mismanagement of prior and present officers of the debtor. The substantial relief prayed for was that the court collect, take charge of, and preserve the assets for both creditors and stockholders.

The State court stockholder's bill was a class bill setting out facts showing the same inability of the debtor to pay claims because of mismanagement of prior and present offi-

cers of the corporation, as set out by the creditors' bill. The stockholder's bill likewise requested the court to collect, preserve and administer the assets of the corporation.

In *Ward* v. *Foulkrod*, 264 Fed. 627, the State court case was a statutory stockholder's bill alleging inability of the corporation to meet its obligations then maturing. The Federal court case was a simple contract creditors' bill, not statutory, alleging inability of the corporation, (admittedly solvent) to provide for its maturing obligations. Both bills prayed for a receiver to conserve the corporation's assets. The Court of Appeals for the Third Circuit sustained the jurisdiction of the State court in which the stockholder's bill was first filed, against the Federal court, though the appointment of a Federal court receiver and actual possession of the property preceded the appointment of the State court receiver.

In the case at bar, the Court of Appeals for the Seventh Circuit misapprehends the nature of the two suits.

It is elementary that a stockholder's suit against a corporation to recover or prevent dissipation of corporate assets is a derivative action (6 Fletcher's Cyc. Corp. 6864). The corporation is therefor the *real party* before the court, and the sole subject mater of the suit is the possession and administration of the corporation's property.

The exact nature of the creditor's bill in the case at bar is not so easy to define.

Whatever rights a simple contract creditor has in the property of a solvent corporation, such rights arise in the course of administration, *after* the property has been taken over by a court of equity. (*Hollins* v. *Brierfield Coal Co.*, 150 U. S. 371.) When the court of equity does take over the corporation's property, new rights are created in the administration by the court of these assets in favor of *all* interested parties, creditors and stockholders, as their interests appear (*Hollins* v. *Brierfield Coal Co.*, 150 U. S. 371).

Who then, is the real party before the Federal court of equity and what is the real subject matter of the suit? To reach a Federal court of equity, the necessary "controversy" and diversity of citizenship is effected through a non-resident creditor having a justiciable claim. Once the corporation becomes a party to such suit, the corporation invokes the court, as a court of equity, *not to satisfy* the justiciable claim of the creditor, but to administer the assets for *all interested* parties. Pending such administration, the plaintiff creditor's right to payment is held in abeyance and is subordinated to his right as one of the interested *cestuis* of the newly created trust (*In re* Metropolitan Receivership, 208 U. S. 90). The real party before the Federal court of equity is the corporation,—the real subject matter of the suit is the administration of the corporation's property.

It follows, even assuming, as, for the purposes of this Point it is assumed, that in law there may be differences in suits short of our Exceptions (*a*) and (*b*), discussed under our Point I, *supra*, which render the doctrine of arrest of property (constructive possession) inapplicable, no such differences exist in the nature of the two suits involved in the instant case.

IV.

The Federal Court was without jurisdiction under Section 37 of the Judicial Code. Under the facts, the instant case does not really and substantially involve a dispute or controversy properly within the jurisdiction of said District Court, and the parties were improperly and collusively joined for the purpose of creating a case cognizable under the Code.

In drawing the line between a case which is collusive and one which is not, this Court has said in *Dawson* v. *Columbia, Etc., Trust Co.*, 197 U. S. 178, that "the decisions on the

two sides of the line are very near to each other." It is a question, therefore, of degree, and the decision in any particular case must depend upon the facts before the court in that case. But this Court has laid down certain general principles by which the conduct of the parties may be gauged in the determination of the issue of collusion:

(1) "So long as no improper act was done by which the jurisdiction of the Federal court attached, the motive for bringing the suit therein is unimportant" (*In Re* Metropolitan Receivership, 208 U. S. 290).

(2) The mere fact that the parties preferred the Federal court to the State court does not show collusion, provided there is no evidence "of any fraud practiced for the purpose of thereby creating a case to give jurisdiction to the Federal court" (*In Re* Metropolitan Receivership, 208 U. S. 290).

(3) "The Court will look beyond the pleadings and arrange the parties according to their sides in the dispute" (*Dawson* v. *Columbia, Etc. Trust Co.*, 197 U. S. 178).

(4) When that is done, and it is found that the real party before the court has done an improper act to procure jurisdiction, or that the real controversy before the court is one which is created to defeat adjudication in the State court, the jurisdiction conferred by the action of the parties on the Federal court is considered collusive (*In Re* Metropolitan Receivership, 208 U. S. 290; *Dawson* v. *Columbia, Etc. Trust Co.*, 197 U. S. 178; *Lord* v. *Vessey*, 8 Howard 251; *Cashman* v. *Amador & Sacramento Canal Co.*, 118 U. S. 38).

Applying these principles to the case at bar we find:

1. The real party before the court is the corporation.

2. The real controversy before the court is the administration of the assets of the corporation for the benefit of stockholders and creditors.

3. There is no collision of interest (controversy) between the real party before the court, the corporation, and the other party, the creditor; the interest of both is identical as to the real controversy.

4. This identical interest of the two parties is antagonistic to the interest of other parties not present in the Federal court.

5. The Federal court jurisdiction is invoked to enforce this common antagonistic interest of both parties against the State court complainant.

6. In invoking this Federal jurisdiction the real party to the controversy improperly acts in fraud of the jurisdiction previously conferred by it upon the State court.

7. In invoking the Federal jurisdiction both parties improperly act in that (*a*) they both have knowledge that the same real controversy is pending in the State court with the corporation as the real party before the State court, and in that (*b*), with full knowledge of such pending controversy in the State court, they invoke Federal jurisdiction to defeat adjudication of that controversy by the State court. Such invocation of Federal jurisdiction this Court says, in *Dawson v. Columbia, Etc., Trust Co.*, 197 U. S. 178, will not be tolerated in the Federal court.

The only substantial relief prayed for, and before the Federal court of equity is itself a fraud on the State court,—the evasion of the effect, in law and in equity, of the corporation's pledge to the State court. It follows that the equity jurisdiction, fraudulently invoked by the corporation through the device of a nominal creditor plaintiff, taints the whole proceeding as collusive.

Both parties in the Federal case contemplated the administration of the assets of the corporation as the real, the substantial relief sought. Although the bill recites (Rec. 3) that

the purpose of the suit is that "of enforcing the claim of complainant," it is obvious that such enforcement of its claim is intended to be through the means specified in the prayer of the bill (Rec. 8) that the assets of the defendant be "declared to be a trust fund to be held and administered for the benefit of the plaintiff and the other creditors and stockholders of said defendant."

That Daniel Boone Woolen Mills, Inc., its officers and counsel, at all times contemplated and sought exactly this general administration of the corporation's affairs in the Federal court, is evident from the fact that the idea of seeking the appointment of a receiver by the Federal court was conceived by the defendant corporation itself (Rec. 103) and that, to this end, it first solicited a stockholder to act as nominal plaintiff and switched to a creditor only on the advice of the non-resident stockholder's counsel that a creditors' bill would be more effective for the corporation's purpose.

The Federal court plaintiff turned over its claim to the counsel, till then, for non-resident stockholders, "for the protection of the company and creditors and stockholders of the Boone Woolen Mills," "for the purpose of having a receiver appointed in the Federal court" (Solomon, Vice President of the deft. Co., Rec. 105-106),—"to apply for a receiver in the Federal Court for the conservation of assets for the benefit of the creditors and stockholders" (Philipson, Chicago Agent of the Fed. Ct. pltf., Rec. 95).

That the Federal court plaintiff merely lent itself to the defendant corporation as an instrumentality to invoke Federal jurisdiction, further appears from facts,—among others, that it moved in the matter only at the solicitation of the defendant corporation, that it made no demand on the defendant corporation for the payment of its supposed debt, and, further, as we contend, that its debt was not even due.

There is not a scintilla of evidence in this record that at the time of the filing of the Federal bill plaintiff's claim was past or presently due, and the sworn bill of complaint herein does not so allege. The bill is so cleverly drawn that an unsuspicious reading does not disclose the pleader's artifice and avoidance of the necessary affirmative showing that the debt was due. (It is elementary that there are no presumptions of jurisdiction, but that the same must affirmatively appear.) The bill alleges (Rec. 3) that the defendant is "indebted" to the plaintiff and refers to the "claim" of the plaintiff, but elsewhere in the bill (Rec. 4) the same, or equivalent terms, are invariably used as referring to non-due items, and whenever the bill mentions presently or past due items (Rec. 4-5) the fact that such items are presently or past due is expressly stated.

It is thus established that the instant suit does "not really and substantially involve a dispute or controversy" between the nominal plaintiff and the defendant, and that "from the very beginning, the suit was and is in reality the suit" (*Cashman* v. *Amador and Sacramento Canal Co.*, 118 U. S. 38) of the Daniel Boone Woolen Mills, Inc., with a party plaintiff "collusively made," "for the purpose of creating a case cognizable" by the Federal court.

V.

Such resort as in the instant case to a Federal court to evade the jurisdiction of a State court, if sustained and maintained, will result in utter disregard of necessary mutual adjustments of power between these two independent judicial systems.

Kline v. *Burke Construction Co.*, 260 U. S. 226, 235.

The importance of the questions presented and the likelihood of their recurrence, merit the issuance of the writ.

Respectfully submitted,

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